

MINUTES
BOARD OF TRUSTEES OF THE
PUBLIC EMPLOYEES' RETIREMENT FUND
143 West Market Street, Suite 500
Indianapolis, IN 46204
December 13, 2002

EXECUTIVE SESSION

Trustees Present

Jonathan Birge, Chair
Richard Doermer, Vice Chair
Garland E. Ferrell
Connie R. Thurman
Nancy Turner

Others Present

Fred Biesecker, PERF Acting Executive Director
Forrest Bowman, Jr., Attorney-at-Law
Mary Beth Braitman, Ice Miller
Ed Gohmann, PERF Legal Counsel
Bart Herriman, Governor's Office
Bruce Kimery, PERF Chief Benefits Officer

The Board met in Executive Session to discuss matters under IC 5-14-1.5-6.1(b)(6).

REGULAR SESSION

Trustees Present

Jonathan Birge, Chair
Richard Doermer, Vice Chair
Garland E. Ferrell
Connie R. Thurman
Nancy Turner

Others Present

Dick Boggs, Burnley Associates
Mary Beth Braitman, Ice Miller
Stephanie Braming, Mercer Investment Consulting, Inc.
Paul Denning, Denning & Co., Green Park
Micah Fannin, Mercer Investment Consulting, Inc.
Diana Hamilton, Special Liaison to the Governor for Public Finance
Bart Herriman, Executive Assistant to the Governor
Pete Keliuotis, Strategic Investment Solutions
Stephanie Rhinesmith, Public Finance Office
Kurt Smith, Strategic Investment Solutions
Eric Swank, Ice Miller
Doug Todd, McCready & Keene, Inc.
Fred Biesecker, PERF Acting Executive Director

Caroline Drum Bradley, PERF Internal Auditor
Diann Clift, PERF MIS Director
Joseph Duncan, PERF Investment Officer
Patricia Gerrick, PERF Chief Investment Officer
Ed Gohmann, PERF Legal Counsel
Bruce Kimery, PERF Acting Chief Benefits Officer
Patrick Lane, PERF Communications Director
Tim Legesse, PERF Investments Officer
Doug Mills, PERF Chief Financial Officer
Tom Parker, 1977 Fund Director
Thomasina Wilson, Investments Assistant
Lynda Duncan, Minute Writer

The Board convened in regular session. A quorum being present, the meeting was called to order.

1. PRESENTATION BY GREENPARK INTERNATIONAL INVESTORS I, L.P.

- a. Green Park International Investors I, L.P. focuses on investments in Global Private Equity Secondaries. A presentation was given by Marleen Groen, Chief Executive Officer, Joanna Jordan, Operations/Investor Relations Director, and Andrew French, Finance Director. This included details of:

- Company background and capital investment strategy;
- Information on Private Equity markets in US and Europe;
- Team composition and expertise;
- Valuation methods;
- Key terms of the partnership.

b. Discussion:

- Mr. Doermer asked if there had been an increase in secondary action coming to the market. He was advised that there had been an increase in the pace of deal flows and approximately 1 – 3% of the capital in the equity market was generated from secondary transactions. Additionally, as a result of the crisis in the ventures market, it had become more recognized for asset and fund managers to use the secondary markets.
- In response to question of location of secondary investments, it was noted that Greenpark had invested in the U.S., and 60% of the capital would occur via deals with European companies with U.S. connections.
- In response to questions on valuation procedures, Greenpark representatives advised that they carried out independent valuations of assets of companies under consideration. This included analyzing all available company data as well as information contained in their own databases. Information is cross-referenced to get the trade sale value potential of each underlying company. Funds being considered for investment must be largely invested. The value is established on a preliminary basis by looking at the quarterly report.

- c. Mr. Birge thanked the Green Park representatives for having come such a long way to give their presentation. He noted that PERF had only recently entered into the business of alternative investments. It was an asset class that was extremely high profile and a possible future investment in this class of approximately \$500 million was anticipated. However, in terms of timing, there were a number of factors that PERF had to take into account, and this is not the appropriate time for PERF to undertake such an investment.

2. APPROVAL OF MINUTES.

MOTION duly made and carried to approve the minutes of the November 8, 2002 Board Meeting.

Proposed by: Nancy Turner
Seconded by: Richard Doermer
Votes: 5 for, 0 against, 0 abstentions

3. ADMINISTRATIVE.

- a. Governor's Economic Development Plan. Mr. Biesecker advised that the administration would encourage PERF and the Teachers' Retirement Fund (TRF) to direct at least \$100 million of alternative investments over the next decade to business ventures in Indiana in the following targeted industry sectors:

- Life Sciences
- Information Technology
- 21st Century Logistics
- Advanced Manufacturing

He noted that this was consistent with PERF's alternative investment policy that had been adopted by PERF's Board of Trustees. Ms Gerrick had provided information at the Investment Committee Meeting on the development of an Indiana Future Fund. That Fund will target investments occurring in Indiana-based companies focusing on life sciences. A Request for Proposal for a Fund Manager will be issued in January 2003.

- b. Search Committee for Executive Director. Mr. Biesecker noted that the next Search Committee meeting would be held on December 18, 2002 to interview a group of semi-finalists. The original pool of 117 applicants had been reduced to a single figure number of semi-finalists. The candidates to be interviewed had been asked to submit a full resume and cover letter. Background checks will be carried out parallel with the interview process. The Committee will aim to recommend a candidate to the Board of Trustees at their meeting on January 10, 2003.
- c. Appointment of Chief Benefits Officer.

MOTION duly made and carried to approve the appointment of Bruce Kimery as the Chief Benefits Officer.

Proposed by: *Garland Ferrell*
Seconded by: *Nancy Turner*
Votes: *5 for, 0 against, 0 abstentions.*

Ms. Turner noted her desire to recommence a regular schedule of Benefits Administration Committee meetings.

d. Staffing Update.

- Mr. Biesecker noted that prior to the Kevin Scott incident, the State Hiring Freeze Committee had given approval for PERF to fill five vacant positions and five newly created positions, and for the conversion of 19 positions from temporary to permanent employees. He noted that PERF had met recently with members of the State Personnel Department to officially add these positions to the PERF staffing table. He noted that PERF was now in the process of filling those positions. Particular emphasis was being made to fill the positions in the Benefits Department because of the backlog of retirement applications and to deal with the workload generated by the State early retirement initiative.
- PERF's Investment Division was requesting additional staff (compliance administrator, investment officer and receptionist). Ms. Gerrick noted that the investment officer would monitor the Treasury Inflation Protected Bond (TIPS) portfolio. The TIPS portfolio can be managed by trading four times a year. PERF currently pays approximately \$100,000 for external management of this portfolio. A portion of the cost associated with this position would be offset by reduction of external management fees. The position would also monitor PERF's external fixed income and securities lending program. This request had not yet been submitted to the State Hiring Freeze Committee. It was the consensus of the Board to approve this requirement for additional personnel.

e. Early Retirement Initiative. This item was tabled for discussion at the next Board meeting in January.

f. Cost of Health Care Adjustment. Since the last Board meeting, the State had announced that health care costs would increase significantly. To offset some of the additional cost to its employees, the State had provided a cost-of-healthcare adjustment of \$1,092 a year. This had been implemented to coincide with the open enrollment period, that started on November 25, 2002, so that employees would have the opportunity to make appropriate health care selections. Mr. Biesecker had been requested by the State Personnel Department to indicate by November 25, 2002 whether PERF intended to participate in this cost-of-healthcare adjustment. PERF members would be impacted by the increases in healthcare costs. Mr. Biesecker noted that the cost of the increase would be met by Funds that the Board had set-aside for employee salary adjustments in the FY 03. After consultation with the Board, PERF had indicated that it would participate in the program. Mr. Ferrell asked if there would be an additional cost to the employee over and above \$1,092 cost-of-healthcare adjustment. He was advised that this would depend on the plan selected, but that in some cases there would be an increase.

g. SIRIS Update. Ms. Clift noted that PERF continued to have concerns about the quality of the product being delivered by Covansys. PERF was withholding payment on approximately \$2.5 million in invoices until items were satisfactorily resolved. Punch lists of items tied to invoices had been developed, relating to items where there was disagreement between Covansys, PERF, and TRF regarding the completion of projects. Invoices would be paid on resolution of pertinent punch list items. The current punch list contains 81 items to be resolved (invoice value of \$200,000) targeted to be completed by December 31, 2002. Members of PERF and TRF meet weekly to evaluate progress. This involves hundreds of individual system changes. PERF and TRF would decide whether to release that portion of the money based on completion of the punch item list by December 31. The Executive Directors of PERF and TRF are working directly with the Vice President of Regional Operations of Covansys to address these issues. Project managers also meet weekly. One of the major issues on the punch-lists concerns quality assurance relating to 1099s. Ms. Clift noted that progress was being made but this was slow going.

- Ms. Turner asked if there would come a point when PERF felt that this company could not fulfill the job, and PERF would turn elsewhere. Ms. Clift noted that the components of the SIRIS system were not proprietary, however the way in which these components were combined was. The system is very customized. Two programmers from the State's centralized processing group were in the process of being trained on how to manage and program the system. This would provide more opportunity to change contractors if required and would enable PERF to manage more of the program itself. The hardware side could be outsourced to another company fairly easily. Mr. Biesecker noted that implementation of a long-term operations and maintenance IT plan would ultimately reduce PERF's reliance on an outside vendor.
- He noted that PERF had been working to develop a record-keeping RFP. Some of the SIRIS functions could ultimately be taken over by this system and the system would eventually maintain the individual ASA balances for all members. With current means, it is impossible to produce figures on a monthly or daily frequency. The record-keeping project had been approved by the Board in conjunction with the custody project.
- Mr. Biesecker noted an anticipated increase in legislative bills relating to providing members the opportunity to change investment direction more frequently. This capability would dovetail with the record-keeping capability. In addition, it would offer day-trading capabilities. Mr. Ferrell asked if this implied that PERF would be running its own TIAA-CREF program. Ms. Turner noted that there was a negative aspect in making it too easy for members to change their investment directions without providing them with the adequate education to make prudent elections. Mr. Ferrell recommended that PERF contact TIAA-CREF to share some of their experiences in this field.
- Mr. Biesecker noted that a short presentation on legislation that has been filed would be presented at the next Board meeting.

4. BENEFITS. Mr. Kimery provided an assessment of the work in progress in the Benefits Department, based on his 30-day tenure as Acting Chief Benefits Officer. In his comments he noted that he had been impressed with the PERF staff.

a. Challenges.

- PERF is recruiting five new retirement counselors and one additional active member counselor. Mr. Kimery noted that even when these posts were filled and counselors trained, this would not be sufficient to deal with the existing workload.
- The SIRIS system did not provide accurate information to develop efficient management tools.
- He provided copies of first generation management reports that had been compiled by eliminating duplicate Social Security numbers, outstanding work products that had finalized retirement dates that had already passed.
- PERF had 462 requests for retirements in various stages of processing. There were also:
 - 63 requests for disability retirement benefits;
 - 29 requests for death and survivor benefits;
 - 494 requests for refunds.
- There were 1,800 new membership records to be processed. Staff members had been working overtime to reduce the backlog. Effective December 12, 374 records had been processed.
- Retirement counselors who meet with members were booked until February 19, 2003.
- Mr. Kimery anticipated receiving numerous requests arising from the State early retirement incentive program. To date, they had received 339 requests for estimates, 184 of which had been completed and forwarded. They had received 22 retirement applications under the program and were forwarding another 82 packages. Plans to handle the additional workload were being discussed.
- The SIRIS system offered additional challenges. All of these are fixable but the system was time-consuming and this hindered the number of retirements that could be processed. The system does not compute length of service and this has to be done manually and the results entered into the system. There is an inability to see the total workload information and this causes frustration among staff members. Error correction is difficult.
- Management reports. PERF is working with Covansys to correct the 1099 issue. because not all of these are being calculated correctly.

- Staff training is inadequate or being done too quickly. More cross training is required. PERF has a minimum number of personnel able to compute length of service without assistance.
- Customer Service. PERF is not providing good customer service due to lack of tools and personnel. There is no formalized customer feedback process.
- Staff members have been released from their duties in other divisions to work on backlogs. However, this means that their normal duties are not being done.

b. Long-term solutions.

- Change Management. A training assessment will be carried out to identify training in operational issues. A presentation to PERF Senior Management will be given on January 7, 2002.
- Use of a third party quality control contractor. Members of PERF Senior Staff will meet to consider alternatives.
- Cross-training. This had been started for refunds staff being trained to do retirement service computation.
- Systems Training. This will be researched at the beginning of the year, following the change management review, in order to review the Fund's business practices.
- Customer Feedback. PERF is considering the possibility of using customer feedback cards.

c. Discussion. Mr. Ferrell asked if overtime costs had been included in the budget. He was advised that under-staffing and unfilled positions plus already budgeted overtime had provided sufficient funds to pay for the overtime in the Benefits Department.

5. ACCOUNTING/FINANCIAL/AUDIT. Mr. Mills provided a comparison of budget year-to-date expenses.

- He noted that the current head-count was 65 full-time staff members. PERF had not used as many temporary employees as forecasted in the budget, and this had freed up funds for the overtime being worked in the Benefits Department. The total for actual expenses for the nine months was just under \$10.9 million, the majority of which was in investment fees for the outside money managers (\$7.3 million). PERF was below budget by approximately 17%.
- Year-to-date expenses for five months of \$10.9 million were 34.8% of the full year budget of \$31.2 million. Most of the significant areas ran favorable to budget.
- Mr. Mills provided a detailed breakdown of some of the more significant line items:
 - Consulting and contractual services. In most cases, PERF was behind where planned for major projects. Projects such as the Asset Liability Study had not

yet started, and this meant that PERF was significantly under budget in consulting services.

- Contractual Services (mainly IT system-related). This represented the cost of outsourcing the IT program. Convansys is responsible for maintaining PERF's new SIRIS system.
- Custodial Services. Mr. Biesecker noted that significant savings were anticipated as a result of the change of custodial services that was due to take place at the end of January.
- Mr. Mills noted that there were some unfavorable variances in certain departments. Postage expenses in accounting (\$20,000 over budget). Currently the entire cost of postage for the PERF postage meter is being charged to the Accounting Department and not allocated to other departments. The most significant postage expenses, related to mailing benefit checks and member statements, are from an outside vendor. These costs are tracked separately and charged to the appropriate department.

6. INVESTMENTS.

- Securities Holdings. Mr. Biesecker referred to a request for information on bond holdings made during the Investment Committee relating to United Airlines. Ms. Gerrick noted that managers strongly advised PERF to continue to hold these equipment trusts. Some of the United Airlines holdings had shown price recovery since the bankruptcy announcement. PERF's United Airlines exposure represented 1.7% of the Reams portfolio. On another downgrade question, she noted managers also strongly recommended holding the Petrofina securities.

7. NEW BUSINESS. There was no new business and the meeting was adjourned.

8. DATE OF NEXT MEETING. The next meeting of the PERF Board of Trustees will be held on Friday, January 10, 2003.